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January 31, 2003

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

VIA HAND DELIVERY

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W., TW-B204
Washington, D.C. 20554

Re: *In re SBC Communications Inc. Request for Initiation of Proceeding into
Character of WorldCom, Inc. and Other Commission Licensees*, RM-10613

Dear Ms. Dortch:

Enclosed for filing in the above-referenced matter please find the original and 4 copies of Statement of SBC Communications Inc. regarding the above-captioned Rulemaking.

Because WorldCom is currently in bankruptcy, SBC has, in an abundance of caution, filed a protective motion with the bankruptcy court to ensure that the automatic stay imposed by 11 U.S.C. §362 does not apply to this filing or, in the alternative, for relief from that stay.¹ If for some reason, the bankruptcy court does not grant that motion, SBC will withdraw this Statement.

I have also enclosed an additional copy of the document for date-stamp and return in the self-addressed envelope provided. Thank you for your assistance in this matter.

Yours truly,


Michael K. Kellogg

Enclosures

¹ Protective Motion Southwestem Bell Telephone, L.P. *et al.*, for Relief from the Automatic Stay To Participate in the Petition for Rulemaking and Request for Initiation of a § 403 Proceeding Into Character of Worldcom, Inc. Filed by the Office of the United Church of Christ, Inc. with the Federal Communications Commission, *In re Worldcom* (S.D.N.Y. Bankr. filed Jan. 31.2003).

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

RM-10613

STATEMENT OF SBC COMMUNICATIONS INC.

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January 31, 2003

INTRODUCTION AND SUMMARY

SBC Communications Inc., on behalf of itself and its subsidiaries (collectively referred to as “SBC”), respectfully submits this statement in response to the Petition for Rulemaking filed by the Office of Communications of the United Church of Christ, Inc. (the “Petition”). SBC agrees that the Commission must undertake a comprehensive investigation of WorldCom’s misconduct. Contrary to what the Petition requests, however, the Commission does not need to initiate a major overhaul **of** its character rules; nor does it need additional enforcement or fining authority; it simply needs to enforce the well-established rules already on the books and apply those rules to WorldCom.

Indeed, given the gravity of the wrongdoing involved, the numerous, egregious and deliberate violations of Commission rules, and the substantial harm to the industry and consumers that has been caused by WorldCom’s misconduct, it is inconceivable that the Commission would not initiate an enforcement investigation into WorldCom’s fraudulent and unlawful acts. If the WorldCom fiasco does not justify a Commission investigation and enforcement action, how could the Commission possibly justify such actions against other companies whose alleged violations pale in comparison to what is already known about WorldCom’s transgressions?

Chairman Powell has recently stated that it is critical “to put some real teeth in our enforcement authority.” and to use remedies that “will have a solid, deterrent effect against illegal activities.”¹ The Chief of the Enforcement Bureau has announced that “if you engage in a serious violation of the Communications Act or the FCC’s rules, there will [] be serious enforcement consequences. . . . The bottom line is that **we** simply aren’t

¹ FCC News Release, *FCC Chairman Michael Powell Outlines **Six** Critical Steps for Telecom Industry Recovery; Calls for Legislation in Three **Areas*** (July 30, 2002).

going to tolerate flagrant violations of the Communications Act and our rules and orders.’’ The Commission must now follow through on these pronouncements and initiate a full and open investigation of WorldCom’s misconduct,

WorldCom and its top executives have already admitted making deliberate and pervasive misrepresentations in their securities filings over a period of several years. WorldCom has submitted those corrupted filings to this Commission. **As** a result, there can be no serious doubt that WorldCom has repeatedly violated the Commission’s rules, which require truth and candor in all filings with the Commission. But the full extent of these violations, and their impact on Commission analyses and deliberations, cannot be known until a full, public investigation has been completed. Such an investigation is clearly required by Commission precedent. Indeed, the Commission has routinely conducted investigations and issued sanctions (up to and including license revocation) for infractions far less significant than those at issue here.

Should the Commission fail to initiate an investigation of WorldCom, it will convey a single, unambiguous message to the telecommunications industry, its investors, and the customers it serves: The Commission will exercise its enforcement authority to investigate and sanction minor infractions of its rules, but will not even investigate instances of massive fraud that have ruinous consequences for the entire industry. Sending such a message, even through inaction, would be very harmful at a time when restoring investor and consumer confidence in the industry is the Commission’s paramount objective.

² David H. Solomon, Chief, Enforcement Bureau, Federal Communications Commission, *Doing Things Differently: The Enforcement Bureau’s First! Year*, Remarks at The New Enforcement Bureau: Nuts, Bolts & Strategies, Washington, D.C. (Sept. 27, 2000) (“Solomon’s Enforcement Bureau Remarks”).

WorldCom's new management, its new accountants, its new lawyers, and its new P.R. flacks, will undoubtedly insist that no investigation is needed because the company is, already, an altogether new company – so much so that it even merits (according to recent reports) a new name.' But until the Commission has conducted a thorough investigation, the Commission cannot have any basis for believing such spin. Corporate attitudes and habits are established over many years. The top-level employees who resigned or were forced out ran WorldCom, hired the managers, established the corporate culture, and inculcated attitudes and business habits for the past five years or more.' If WorldCom is allowed to proceed on its own say-so that all is now well, the industry and its investors will inevitably conclude that, at the Commission, inertia and familiarity override legal duty, ethical principle, character, integrity, probity, and the public interest, so much so that the Commission will not even bother to ask questions, still less impose sanctions, when the malefactors and the infractions get big enough.

WorldCom's new management will undoubtedly also contend that WorldCom is simply too big and too important to be subjected to an investigation that could, potentially, threaten the revocation of all its Title II and Title III licenses. But size cannot

³ Dow Jones Newswires, *WorldCom Considers Name Change*, Wall St. J. Online, Jan. 13, 2003.

⁴ Bernard Ebbers was named president and CEO of LDDS, the predecessor to WorldCom, in 1985. See Mark Ribbing, *Upstart GUM the Distance*, Sun (Baltimore), Nov. 16, 1997, at ID. Former CFO Scott Sullivan joined WorldCom in 1992 as vice president and assistant treasurer, following WorldCom's acquisition of Advanced Telecommunications Corp. WorldCom Press Release, *WorldCom, Inc. Appoints New Board Member* (Mar. 12, 1996). Former controller David Myers served as senior vice president and controller of WorldCom since August 1995. Complaint ¶ 1, *SEC v. Myers*, Civ. No. 02CV7749 (JSR) (S.D.N.Y. filed Sept. 26, 2002). Former director of management reponing Betty Vinson had been employed by WorldCom since 1996. Complaint ¶ 14, *SEC v. Vinson*, Civ. No. 02CV8083 (JSR) (S.D.N.Y. Filed Oct. 10, 2002) ("*SEC v. Vinson* Complaint"). Buford Yates had served as WorldCom's Director of General Accounting since 1997. Joseph Radigan, *Line Charges: Ex-WorldCom CFO Indicted*, CFO.com Aug. 29, 2001, at <http://www.cfo.com/article/1,5309,7610,00>. Former Director of Legal Entity Accounting Troy Normand had been employed in the General Accounting Department since 1997. *SEC v. Vinson* Complaint, ¶ 15. See also Neil Weinberg, *Ring of Thieves*, Forbes, June 10, 2002, at 64 (Walter Pavlo, a former MCI employee serving time for obstruction of justice, money laundering, and mail fraud, says he "cooked the books, under pressure from higher-ups, to help bolster MCI's growth.").

be a defense in such matters. If the peccadilloes of small companies are sanctionable, so too must be the massive and deliberate fraud of a large company. The Commission cannot shrink from its responsibility to investigate such fraud simply because the conduct is so grave as to warrant, potentially, the gravest of sanctions.

That would be true, moreover, even if the end result of the investigation were the dismantling of WorldCom's business. As one leading industry analyst recently concluded, WorldCom is "more a shopping mall of products and services rather than a department store. Like many large enterprises, WorldCom's history is rooted in merger and acquisition, but unlike global behemoths like Deutsche Bank and Sony, or even industry peers like, Verizon and SBC, WorldCom has done little to integrate its divisions and operating units into a monolithic entity." Potential buyers of WorldCom's assets include IDT (which acquired WinStar's assets), Level 3 (which, with the backing of Warren Buffet, recently acquired Genuity), ALLTEL, and AT&T (which has already taken on WorldCom's former share of Internet traffic), as well as the Bell Companies.⁶

As Commission Chairman Powell recently observed, the industry's overall survival and health going forward will "depend on prudent industry consolidation."⁷ It may well be that that inevitable process of consolidation should start with the dissolution and sale of the company that perpetrated a \$9-billion (and counting) fraud at the highest levels of the company on investors, financial regulators, suppliers, competitors,

⁵ Eastern Management Group. *Is WorldCom Too Big to Fail? Liquidation Could Improve Telecom Sector* 4 (2003) ("EMG Report").

⁶ See *id.* at 5

⁷ Michael K. Powell, Chairman, Federal Communications Commission, Financial Turmoil in the Telecommunications Marketplace: Maintaining the Operations of Essential Communications, Statement Before the Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C. (July 30, 2002).

customers, and this Commission. It may well be, in other words, that the public interest will **be** best served by the orderly sale of WorldCom's businesses. Certainly, the public interest will be ill-served if the Commission winks at WorldCom's unprecedented fraud and fails even to open a full, public investigation.

Finally, the Commission owes no deference to the bankruptcy court in deciding, after a full investigation, whether revocation of WorldCom's licenses or some other appropriate sanction will best serve the *public* interest here. A bankruptcy court looks to the immediate interests of creditors and employees, but has no mandate to evaluate broader impacts on the industry as a whole. The Commission, by contrast, may – and indeed must – consider those effects. A bankruptcy court does not investigate and penalize violations of the Commission's rules. The Commission can – and, if those rules are to maintain their integrity, must – do so.

Nor does the Supreme Court's recent *Nextwave* decision⁸ affect the Commission's enforcement authority, including its ability to revoke licenses for misconduct, while WorldCom is in bankruptcy. The sole basis for revoking WorldCom's licenses – if the Commission, after a full investigation, reaches such a decision – would be WorldCom's fraudulent misconduct, whereas the bankruptcy code prohibits revocation only where “the failure to pay a dischargeable debt [is] *alone* . . . the proximate cause of the cancellation.” *Nextwave*, slip op. at 8 (emphasis added).

⁸ *FCC v. Nextwave Personal Communications Inc.*, Nos. 01-653 & 01-657, 2003 U.S. LEXIS 1059, at *16 (Jan. 27, 2003).

I. WorldCom's Fraud Was Uniquely Large and Harmful.

Telecommunications is a complex industry, and it is not unusual for companies to fall short of perfect compliance with the Commission's many, complex rules. But WorldCom did not "fall short"; it engaged in prolonged and systematic fraud that corrupted its relations with this Commission, securities regulators, investors, customers, and every other major carrier in the industry. WorldCom's fraud was indeed so far-reaching – and has thus been so widely publicized – that it is not necessary to recapitulate it in great detail here, nor to dwell on the fact that there may well be much more yet to be exposed if and when the Commission investigates this matter further.

From what has been revealed so far, ' we know that the company's accounting swindles for 1999 through the first quarter of 2002 resulted in earnings being misstated by an amount in excess of \$9 billion – the largest accounting fraud in U.S. history." As one analyst has observed, "nothing comes close to the WorldCom fraud." The United States Attorney General has compared the miscreants to "common thieves." The President of the United States has described WorldCom's conduct as "egregious."¹³

⁹ On January 30th the New York Times reponed that WorldCom's sales "withered far faster in the second half of 2002 than lhe company has publicly reponed." S. Schiesel, *WorldCom Sales Dropped Faster Than Reported*, N.Y. Times (Jan, 30, 2003); *see also* Boycott WorldCom, *2002 Pipeline Trending Report* (Jan. 13, 2003). <http://www.boycottworldcom.com/2002trendreport.htm>.

¹⁰ *See* WorldCom Press Release, *WorldCom Says Additional Restatements Likely* (Nov. 5, 2002); *WorldCom's Sullivan Can Afford New York Trial, Prosecutors Soy*, Wall St. J. Online (Dec. 25, 2002). In November 2002, WorldCom consented to enter a permanent injunction to resolve claims brought by the SEC's civil lawsuit regarding WorldCom's past accounting practices. *See* WorldCom Press Release, *WorldCom Gains Settlement with SEC* (Nov. 26, 2002).

¹¹ Pia Sarkar. *Year in Review, People in Crisis; WorldCom Unravels; Ex-CEO Bernie Ebbers Flew High. Fell Hnrd and Took the Telecom Giant with Him*, S. F. Chron., Dec. 27, 2002, at B1 (quoting Guzman and Co. analyst Patrick Comack).

¹² John Ashcroft, United States Attorney General, Remarks at the WorldCom Press Conference (Aug. 1, 2002).

¹³ White House Press Release, *Corporate Responsibility: President Promises Worldcom Investigation* (June 26, 2002) (excerpts from President Bush and Prime Minister Blair press release).

A fraud of this magnitude was not the work of one rogue or lower-level employee somewhere deep in the catacombs of the company. Four of WorldCom's top financial employees have already plead guilty to fraud charges¹⁴; its former chief financial officer has plead not guilty to six felony counts, but has reportedly offered to testify against former president and CEO Bernie Ebbers.¹⁵ According to special examiner (and former Attorney General) Richard Thornburgh, "[t]here were numerous failures, inadequacies and breakdowns in the multilayered system designed to protect the integrity of the [company's] financial reporting system at WorldCom, including the board of directors, the audit committee, the company's system of internal controls and the independent auditors.'"

The harmful impacts of this corporate-wide collapse have extended very far indeed. Investors have – quite understandably – lost confidence in the entire industry, Hordes of WorldCom shareholders, who – less than four years ago – believed themselves to be holding equity in a company worth \$120B (at its peak) – have seen their investments wiped out completely. JP Morgan Trust Company is apparently left holding

¹⁴ Controller David Myers pleaded guilty to one count each of conspiracy to commit securities fraud, securities fraud, and making false filings with Securities and Exchange Commission. Betty Vinson, the former director of management reponing, entered her plea to one count of securities fraud and one count of conspiracy to commit securities fraud in the United States District Court in Manhattan. Troy Normand, the director of legal entity accounting, pleaded guilty to conspiracy and securities fraud for his part in the same scheme. Buford Yares Jr., accounting director, pleaded guilty to one count of conspiracy to commit securities fraud and one count of securities fraud. *WorldCom Exec Pleads Guilty*, CNNmoney.com (Sept. 26, 2002), at http://money.cnn.com/2002/09/26/news/worldcom_myers/; *2 More WorldCom Execs Plead Guilty*, CBSNews.com (Oct. 10, 2002), at <http://www.cbsnews.com/stories/2002/11/05/national/main528148.shtml>; *Ex-WorldCom Exec Pleads Guilty*, CNNmoney.com (Oct. 7, 2002), at <http://money.cnn.com/2002/10/07/news/worldcom/>.

¹⁵ See Robert Schoenherger, *Sullivan Offers Info on Ebbers*, Clarion-Ledger (Jackson, MS), Dec. 22, 2002, at C1; *WorldCom's Sullivan Can Afford New York Trial, Prosecutors Say*, Wall St. J. Online (Dec. 25, 2002); Laurie P. Cohen & Deborah Solomon, *WorldCom Ex-CFO Fails To Link Ebbers to Fraud*, Wall St. J. (Dec. 20, 2002).

¹⁶ Barbara Powell, *WorldCom Fraud Called Bigger Than \$7 Billion*, Chattanooga Times/Chattanooga Free Press, Nov. 5, 2002, at C1

\$17.2B in uncollectible bond debt.” The pension funds of twelve states that are now suing WorldCom have lost between \$2 billion and \$3 billion.¹⁸ According to one analyst, “[d]estruction of investor confidence of this magnitude hasn’t occurred in roughly 70 years.”¹⁹

The Regional Bell Companies – which are required, by Commission rules, not only to interconnect with WorldCom but also to extend it credit” – have been left holding debts that may never be paid: SBC is owed more than \$600 million, and each of the other Bell companies is owed hundreds of millions as well.

Less obviously, but even more fundamentally, every other carrier in the industry has been forced to buy equipment, hire employees, and set prices in tandem or in direct competition with a carrier that was printing its own money, so to speak. While the Commission and other regulators – under the express mandate of the 1996 Telecom Act – labored to eliminate subsidies and rationalize the industry’s complex system of

¹⁷ Consolidated List of Creditors Holding 50 Largest Unsecured Claims, *WorldCom, Inc., et al.*, Bankruptcy Petition No. 02-13533 (Bankr. S.D.N.Y. filed July 21, 2002) (“Consolidated List of Creditors”). Other creditors with over \$2 billion in bond debt include Mellon Bank (\$6.6B), Citibank (\$3.3B), JP Morgan Chase (\$3.0B), Bear Stearns (\$2.78), Bank of New York (\$2.60), and State Street Bank (\$2.0B). *Id.*

¹⁸ *NYS Comptroller McCall Sues WorldCom*, **Andersen**, Reuters (July 2, 2002); *The Power of the Purse. How Investors Can Restore Integrity to Our Financial Markets*, Phil Angelides, California State Treasurer (2002) (California: \$850 million); Gary Susswein, *Kirk: Cornyn Unfit for WorldCom Role*, Austin American Statesman, Sept. 24, 2002, at B1 (Texas: \$235 million); David Glovin, *WorldCom Ordered to Provide Documents*, Times Union (Albany, NY), Nov. 22, 2002, at E4 (New York: \$306 million); Amy J. Bryson, *Pension Shortfall Pinches Budget*, Deseret News (Salt Lake City, UT), Dec. 28, 2002, at B01 (Ohio: \$206 million in state pension fund; \$100 million in teachers’ retirement fund; Michigan: \$116 million; North Carolina: \$100 million); Barbara De Lollis, *Bidding War Starts for US Airways*, USA Today, Sept. 20, 2002, at 5B (Alabama: \$300 million); Rebecca Cooke, *Washington State Sues to Recover WorldCom Losses*, Associated Press State & Local Wire, Nov. 5, 2002 (Washington: \$100 million; Florida: \$85-90 million); *Pension Funds Sue WorldCom, Enron* (Sept. 2002) (Maryland: \$52 million; Massachusetts: \$25 million), at <http://www.massretirees.com/investment/pensionfunds0902.html>; *Week in Review*, Milwaukee J. Sentinel, Dec. 8, 2002, at 02D (State of Wisconsin Investment Board (\$40 million) and City of Milwaukee Employees’ Retirement System (\$10 million)); Chris H. Sieroty, *State Pensions Hurt by WorldCom*, Washington Times (June 27, 2002) (Illinois: \$33 million).

¹⁹ Frederick P. Gabriel, Jr., *Reverse Spin: WorldCom Hangs Up on Integrity*, Investment News, July 1, 2002, at 4.

²⁰ See 11 U.S.C. § 365(e).

interdependent prices, WorldCom simply erected a massive new system of subsidies all its own, at the expense of its shareholders and debtors. AT&T,²¹ Sprint,²² Verizon, SBC, BellSouth, Qwest, and other major long-distance carriers have had to match WorldCom's fraud-subsidized prices.

As a direct consequence, investment analysts now see "an entire industry" that is severely "overcapitalized," and that "strains under a capacity load that just doesn't make sense."²³ Capacity utilization – "simply put, the amount of stuff companies have lying around that they're actually using" – fell to a "stunningly low" 49.9 percent in September 2002, according to one analyst, citing a Federal Reserve estimate.²⁴ And as the Federal Reserve itself reports, "[e]xcess capacity in the provision of telecom services is continuing to weigh heavily on the demand for communications equipment."²⁵ The destructive aftermath of gross over-investment in capital plant paid for with misappropriated money will continue to be felt for years, and quite possibly decades, whatever the Commission now does with respect to WorldCom.

²¹ According to AT&T chairman and CEO David Dorman the frauds "distorted costs and prices, growth, and value." Martha McKay, *AT&T Bears Expectations — But Just Barely: Cable Profits Offset Long-Distance Woes*, Record (Bergen County, NJ), Oct. 23, 2002, at B1.

²² Sprint chairman and CEO Bill Esrey says his company and others were forced to match WorldCom's pricing, and that Sprint alone lost more than \$500 million matching prices that WorldCom kept low through fraudulent accounting. David Hayes, *WorldCom Hurt All, Esrey Says; Sprint Chief Laments 'RippleEffect' on the Industry*, Kansas City Star, Oct. 8, 2002, at D10; Bill Esrey, CEO, Sprint Corp., Remarks at Yankee Group Telecom, New York, NY (Oct. 21, 2002).

²³ Justin Lahart, *Telecom: Worse Than You Thought*, CNNMoney.com (Nov. 12, 2002), at <http://money.cnn.com/2002/11/11/markets/zombietelcos/> (quoting Credit Suisse First Boston chief investment officer Paddy Jilek).

²⁴ *Id.*; Federal Reserve, *Statistical Release: G.17 (419) Indus. Prod. & Capacity Utilization* at Table 7 (Dec. 17, 2002).

²⁵ Board of Governors of the Federal Reserve System, *Monetary Policy Report to the Congress* at 12 (July 16, 2002).

II. A Full-Scale Enforcement Investigation of WorldCom Is Warranted Under the Commission's Established Precedent.

Well-settled precedent requires the Commission to initiate a full and open investigation to determine the extent to which WorldCom's misconduct violated Commission rules and other federal laws, whether WorldCom remains fit to retain its Commission-issued licenses, and whether other sanctions are appropriate.

As both the Commission²⁷ and the courts²⁸ have emphasized, the regulatory process simply cannot function if the Commission loses trust in its licensees. The Commission has accordingly adopted character-qualification requirements for licensees that place a very strong emphasis on character and probity.²⁸ "[M]isrepresentation to the Commission is always an egregious violation."²⁹

As described in Part I above, WorldCom and its top executives have already admitted making deliberate and pervasive misrepresentations in their earnings statements

²⁷ See, e.g., *Contemporary Media, Inc.*, Decision, 13 FCC Rcd 14437, 14454, ¶ 34 (1998) ("The requirement for absolute truth and candor for those appearing before the Commission is bedrock because the Commission must rely heavily on the completeness and accuracy of the submissions made to it by applicants who, in turn, have an obligation to provide the Commission with the facts needed to carry out its statutory mandate."); *Fox River Broad., Inc.*, Order, 93 F.C.C.2d 127, 130, ¶ 7 (1983) ("Our concern with misrepresentation and lack of candor stems from the necessity of relying on licensees' representations to the Commission."); *Revocation of the Licenses of Pass Word, Inc.*, Order to Revoke Licenses, to Terminate Comparative Proceedings, and to Proceed with Docket 20941, 76 F.C.C.2d 465, 519, ¶ 121 (1980) ("There is no question that revocation is an appropriate remedy under the Act where there has been a repeated pattern of deliberate misrepresentation and concealment to this Commission."); see generally *Sea Island Broad. Corp.*, Decision, 60 F.C.C.2d 146 (1976).

²⁸ See, e.g., *Garden State Broad. Ltd. P'Ship v. FCC*, 996 F.2d 386, 393 (D.C. Cir. 1993) ("Deliberate failures to produce information can result in disqualification for lack of candor."); *Lorain J. Co. v. FCC*, 351 F.2d 824, 830 (D.C. Cir. 1965) ("[a] cardinal assumption of the regulatory system is undercut by a pattern of false or evasive reports"); *Applications of Valley Broad. Co.*, Decision, 4 FCC Rcd 2611, 2612, ¶ 4 (1989) (misrepresentation and lack of candor are very serious offenses in Commission proceedings, and can be fatal in license renewal (or license revocation) cases); see generally *FCC v. WOKO, Inc.*, 329 U.S. 223 (1946).

²⁹ See *Policy Regarding Character Qualifications in Broadcast Licensing*, Report, Order, and Policy Statement, 102 F.C.C.2d 1179, 1209-10, ¶¶ 54-57 (1986) ("*Character Policy Statement*").

³⁰ *The Commission's Forfeiture Policy Statement and Amendment of Section 1.80 of the Commission's Rules to Incorporate the Forfeiture Guidelines*, Report and Order, 12 FCC Rcd 17087, 17144, ¶ 21 (1997).

over a period of several years. These admissions alone strongly suggest that WorldCom violated a number of the Commission's rules. Section 1.785(a) requires all publicly traded companies to submit to the Commission "verified" copies of the annual financial statements they file with the Securities and Exchange Commission.³⁰ Section 54.711 requires carriers providing interstate telecommunications services to file a Telecommunications Reporting Worksheet (FCC Form 499) twice a year." And Section 1.17 requires truthful written statements in all filings with the Commission.³²

WorldCom may perhaps argue to the Commission that such financial filings are merely pro forma – and that the Commission has no reason to concern itself about false financial statements because securities regulators already do so. The Commission, however, must carefully consider just how pervasively the gigantic myth of WorldCom's financial health has colored Commission findings and orders for as far back as the frauds may have extended, **As** a starting point, the Commission should require WorldCom to identify each pleading, letter, application, **ex** parte, affidavit and other document that it filed with the Commission in the last five years that was inaccurate or misleading.

1. In the past five years, the Commission has conducted major proceedings concerning rates paid by or to long-distance carries, including access charges³³ and

³⁰ See 47 C.F.R. § 1.785(a); see also *id.* § 43.21(b)

³¹ See *id.* § 54.711; see also *id.* § 54.713

³² See *id.* § 1.17

³³ See, e.g., *Access Charge Reform*, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962 (2000) (adopting the CALLS proposal and ordering an immediate \$3.2 billion reduction in access charges paid by long distance companies); *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, 16 FCC Rcd 19613, 19689-96, ¶¶ 179-193 (2001) (declining to adopt several requirements for interexchange carriers proposed by the Multi-Association Group ("MAG")).

contributions to universal service.³⁴ The knowledge that the second largest long-distance carrier was rapidly headed toward bankruptcy would undoubtedly have been highly relevant to the Commission's deliberations in these multi-billion-dollar proceedings. Until the Commission has conducted a full investigation, it cannot know just how much it may have relied on the false numbers filed by WorldCom in those proceedings.

2. In the past five years, the Commission has made a series of major decisions affecting new competitive entry into long-distance markets – most notably in its section 271 proceedings. Both before the Commission, and in the wider public debate, it has been repeatedly argued that long-distance markets didn't really “need” new entry by the Regional Bell Companies because competition was already robust.³⁵ In both section 271 proceedings and the Triennial Review proceedings, WorldCom has submitted extensive information about its own costs and profitability – much of which, it is now clear, was false.” More generally, the knowledge that the second largest long-distance carrier was rapidly headed toward bankruptcy would certainly have been relevant to the

³⁴ *Federal-State Joint Board on Universal Service*, Tenth Report and Order, 14 FCC Rcd 20156 (1999) (adopting input values for the Commission's model for estimating non-rural carriers' forward-looking costs); *Federal-State Joint Board on Universal Service*, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432 (1999) (adopting the methodology to be used to compute non-rural carriers' revised support amounts); *Federal-State Joint Board on Universal Service*, Report and Order on Reconsideration, 16 FCC Rcd 5748, 5748, ¶ 2 (2001) (revising the methodology used to assess carrier contributions by shortening the interval between the accrual of revenues and assessment based on those revenues, improving the existing methodology by basing assessments “on revenue data that are more reflective of current market conditions”).

³⁵ See, e.g., Comments of MCI WorldCom, Inc., on the Application by SBC for Authorization To Provide In-Region, InterLATA Services in Texas at 93, *Application by SBC Communications Inc., et al. for Provision of In-Region, InterLATA Services in Texas*, CC Docket No. 00-4 (FCC filed Jan. 31, 2000) (noting the “already robustly competitive long distance market”).

^{1b} See, e.g., Declaration of Vijetha Huffman on Behalf of WorldCom, Inc. ¶ 6, attached to Comments of WorldCom, Inc. on the Application by Verizon for Authorization To Provide In-Region, InterLATA Services in Vermont, *Application of Verizon New England for Authorization To Provide In-Region, InterLATA Services in Vermont*, CC Docket No. 02-7 (FCC filed Feb. 6, 2002) (estimating WorldCom's internal costs of providing local service); Ex Parte Letter from Gil M. Strobel, Lawler, Metzger & Milkman, LLC, representing WorldCom, Inc., to Marlene H. Dortch, Secretary, FCC, CC Docket Nos. 01-338, et al. (Jan. 8, 2003) (attaching an analysis estimating costs WorldCom would incur in serving residential customers using its own switches).

Commission's deliberations in proceedings so directly affecting the market structure of the long-distance industry.

3. **As** part of the September 1998 approval of the MCI/WorldCom acquisition, the European Commission, the Department of Justice, and the Commission imposed a condition requiring the spin-off of the Internet business, including a backbone network, formerly owned by MCI.³⁷ Until the Commission has conducted a full investigation, it cannot know how, if at all, WorldCom's accounting frauds influenced the terms of those conditions, or influenced WorldCom's negotiations with Cable & Wireless, which eventually acquired the spun-off property. It has since been alleged that WorldCom divested these Internet assets in such a manner as to "threaten to impair Cable & Wireless's competitiveness."³⁸ Following the spin-off, Cable & Wireless "spent a year recruiting and training employees and [] announced a nearly \$700 million investment into the network to make up for the setbacks caused by MCI WorldCom's refusal to honor their commitments." Cable & Wireless recently underwent a major restructuring, which included reducing its presence in cities in the United States and Europe, laying off 3,500 employees, and closing a number of data centers.⁴⁰

³⁷ *Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, Memorandum Opinion and Order, 13 FCC Rcd 18025 (1998).

³⁸ See Testimony of Mike McTighe, CEO, Cable & Wireless, Global Operations, Before the Senate Comm. on Commerce, Science and Transportation, Hearings on Mergers in the Communications Industry, 106th Cong., 1st Sess. (Nov. 8, 1999) ("McTighe Testimony"), available at 1999 WL 1022955 (MCI WorldCom divested MCI's Internet business in such a way as to "threaten to impair Cable & Wireless's competitiveness"); see also Complaint ¶¶ 37-40, *Cable & Wireless USA, Inc. v. MCI WorldCom, Inc.*, Civil Action No. 99-204 (D. Del. filed Mar. 31, 1999).

³⁹ Mike McTighe, Chief Executive Officer, Cable & Wireless, Global Operations, Testimony before the Senate Commerce, Science, and Transportation Hearing on Mergers in the Communications Industry (Nov. 11, 1999).

⁴⁰ See, e.g., Denise Pappalardo & Jennifer Mears, *Cable & Wireless De-Emphasizes Its U.S. Business*, Network World (Nov. 18, 2002), at <http://www.nwfusion.com/news/2002/1118cwreorg.html>. The Commission recently granted Cable & Wireless's application to discontinue providing domestic voice

4. In the past five years, the Commission has issued numerous orders affecting Internet access markets, and has addressed numerous requests from Bell Companies for relief from restrictions on the provision of data services across LATA boundaries.” All of these decisions would surely have been influenced by the knowledge that the industry’s largest backbone carrier of Internet traffic was headed for bankruptcy.

5. The WorldCom/Sprint merger was proposed in October 1999 and terminated – as a result of strenuous regulatory opposition – in July 2000. The Commission subsequently approved WorldCom’s acquisition of Intermedia in January 2001, after WorldCom had reached a settlement with the Department of Justice to divest Intermedia’s assets, including its Internet backbone.” Regulatory review of both of these proceedings would surely have been significantly influenced by the knowledge that WorldCom was heading rapidly for bankruptcy.” On the one hand, antitrust law

services to its dedicated access customers in 41 states and the District of Columbia. See Section 63.71 *Application to Discontinue Cable & Wireless USA, Inc. Application to Discontinue Services*, Order ¶ 2, Comp. Pol. File No. 624, DA 02-3603 (rel. Dec. 27, 2002).

⁴¹ See, e.g., *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor, to AT&T Corp., Transferee*, Memorandum Opinion and Order, 14 FCC Rcd 3160, 3194 ¶ 69 (1999) (noting in evaluating the AT&T/TCI merger that “MCI-WorldCom is the leading provider of the facilities and transport services used to support dial-up services.”); *Applications for Consent to the Transfer & Control of Licenses and Section 214 Authorizations by Time Warner Inc. and America Online, Inc., Transferors, to AOL Time Warner Inc., Transferee*, Memorandum Opinion and Order, 16 FCC Rcd 6547 (2001); *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Memorandum Opinion and Order, and Notice of Proposed Rulemaking, 13 FCC Rcd 24011 (1998); *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Second Report and Order, 14 FCC Rcd 19237 (1999); *Internet Compensation for ISP-Bound Traffic*, Order on Remand and Report and Order, 16 FCC Rcd 9151 (2001) (concluding that telecommunication traffic delivered to an ISP is “information access” that is not subject to reciprocal compensation).

⁴² *Intermedia Communications Inc., Transferor, and WorldCom, Inc., Transferee, for Consent to Transfer Control of Corporations Holding Commission Licenses and Authorizations Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 21, 63, 90, 101*, Memorandum Opinion and Order, 16 FCC Rcd 1017 (2001). Under the settlement agreement, WorldCom would retain capital stock of Digex, a web-hosting business.

⁴³ As one market analyst has subsequently remarked of the WorldCom/Sprint acquisition, “[o]ne can only wonder if that [would] be allowed today in this kind of current environment.” *Senators To Quiz*

recognizes a “failing firm” doctrine⁴⁴; on the other hand, it can hardly serve the public interest to merge a small but financially sound company into a much larger company that is hopelessly insolvent.⁴⁵

At an absolute minimum, the Commission must investigate the extent to which WorldCom’s admitted misrepresentations not only violated the Commission’s rules, but affected policies framed, rules issued, and transactions approved or rejected, on the basis of severely incomplete information about the true state of competition in long-distance voice and data markets. The Commission has the statutory authority to investigate alleged violations of its rules.⁴⁶ The Commission routinely uses that authority, and does so to investigate infractions far less significant than WorldCom’s.⁴⁷ No other regulatory

FCC’s Powell, Telecom Execs About Continuity of Service, CNNfn, Market Call, Transcript # 073001cb.105 (July 30, 2002) (quoting Bruce Francis, Sr. Technology Correspondent, Market Call).

⁴⁴ U.S. Department of Justice and Federal Trade Commission, **Horizontal Merger Guidelines § 5.1** (rev. Apr. 8, 1997).

⁴⁵ In hindsight, it is clear that WorldCom’s filings with the Commission in the Intermedia merger were indeed false and misleading and were intended to convey the impression that WorldCom was financially healthy. See *Intermedia Communications Inc., Transferor, and WorldCom, Inc., Transferee, for Consent To Transfer Control of Corporations Holding Commission Licenses and Authorizations Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 2, 63, 90, 101*, Application for Consent to Transfer Control, CC Docket No. 00-206, at 6-7 (FCC filed Oct. 23, 2000) (stating that the merger was “critical for Digex’s future growth and development” because it would provide Digex “access to WorldCom’s capital” and would provide Intermedia “access to financing needed for capital expenditures and operating expenses”); *id.* at Att. E, Agreement and Plan of Merger, § 3.6 (stating that WorldCom’s financial statements filed with the SEC complied “in all material respects with the accounting rules. [had been] prepared in accordance with GAAP . . . and fairly present[ed] in all material respects the consolidated financial position of [WorldCom] and its consolidated Subsidiaries”).

⁴⁶ See 47 U.S.C. §§ 154(i), 154(j), 208, 218, 403; **Rules and Policies on Foreign Participation in the U.S. Telecommunications Market**, Order and Notice of Proposed Rulemaking, 12 FCC Rcd 7847, 7898, ¶ 125 (1997) (“We . . . have ample authority to investigate allegations that a carrier has violated our rules.”).

⁴⁷ See, e.g., **Leslie D. Brewer; Licensor of Amateur Radio Station and General Class Operator License KC4HAZ; Licensee of Station KAE1170 in the General Mobile Radio Service**, Order To Show Cause, Notice of Order of Suspension, Notice of Opportunity for Hearing, and Notice of Apparent Liability for a Forfeiture, 16 FCC Rcd 5671 (2001) (suspending an amateur radio operator’s license and commencing a hearing proceeding before an FCC ALJ to determine whether licenses should be revoked); *Peninsula Communications, Inc.; Former Licensee of FM Translator Stations K285EF, Kenai, Alaska; K283A B, Kenai/Saldoma, Alaska; K257DB, Anchor Point, Alaska; K265CK, Kachemrk City, Alaska;*

agency can conduct this investigation in the Commission's place. As Congress has recognized, only the Commission itself is qualified to investigate how violations of the Commission's rules affect the regulatory process and the public interest.⁴⁸ Commission rules delegate that investigatory process to the Enforcement Bureau." And the Chief of the Enforcement Bureau recently declared in no uncertain terms that "if you engage in a serious violation of the Communications Act or the FCC's rules, there will [] be serious enforcement consequences."⁵⁰

III. A Full Investigation and Appropriate Sanctions Are Necessary To Forestall Further Damage from WorldCom's Misconduct and To Restore Confidence in the Telecommunications Industry.

The harm that WorldCom has done to the competitive structure of the industry and to investor confidence cannot be ignored. A Chapter 11 reorganization may restore WorldCom's own books to good health, but it won't restore the industry's. As a CEO of a small CLEC observed last July, "It's starting to seem like Chapter 11 is like going to a car wash: The companies go in, they get their debt hosed off and they come back. It's really quite disheartening."

WorldCom itself is apparently already counting on a car-wash outcome. On January 14, the company issued a press release announcing a series of initiatives directed

K272CN, Homer, Alaska, and K274AB and K285AA, Kodiak, Alaska, Notice of Apparent Liability for Forfeiture and Order, 16 FCC Rcd 16124, 16124, ¶ 1 (2001) (finding an Alaskan FM translator operator liable for a \$140,000 forfeiture for failing to cease operations as ordered, and noting that continued unauthorized operation "may lead to an order to show cause to revoke [the operator's] other Commission licenses.").

⁴⁸ See 47 U.S.C. § 403.

⁴⁹ See 47 C.F.R. § 0.111.

⁵⁰ Solomon's Enforcement Bureau Remarks.

⁵¹ Mark Reilly, *CEO: Bankruptcy Hurts the Solvent*, Minneapolis Bus. J., July 26, 2002 (quoting Onvoy CEO Janice Aune), at <http://twincities.bizjournals.com/twincities/stories/2002/07/29/story3.html?storyid=318>.

at local and long-distance consumer markets that – according to the company’s CEO – will “generate 1 million new Neighborhood sales and 2.5 million new consumer long-distance sales over the next 100 days.” Citing an “outrageous sense of urgency,” Mr. Cappellas stated, “we have the opportunity to attack the marketplace like never before.”⁵² WorldCom’s representatives appear to be slamming customers and engaging in deceptive marketing practices.⁵³ How convenient it must seem to WorldCom’s new management, to be able to “attack . . . like never before,” in full possession of both licenses and networks, applied for and purchased with fraudulently incurred debts, and wholly unencumbered by the obligation to pay off any of those same debts, or even to answer to millions of shareholders, who have little incentive to vote their now valueless shares.

The Commission, however, has a grave statutory responsibility to determine whether permitting WorldCom to retain its licenses is in the public interest. As described in Part IV below, the bankruptcy court overseeing WorldCom’s reorganization looks only to the immediate interests of creditors and employees, but has no mandate to evaluate broader impacts on the industry as a whole. This Commission may and must.

That process must start with a full investigation of WorldCom’s misconduct. And once the Commission has conducted a full investigation of WorldCom, it will have to determine whether WorldCom deserves to retain its licenses, or whether they should be

⁵² WorldCom Press Release, *WorldCom Announces Key Initiatives for First 100 Days* (Jan. 14, 2003) (quoting chairman and CEO Michael Capellas).

⁵³ See, e.g., Press Release of the Wisconsin Governor’s Office, *First No Call List Case Referred to Attorney General’s Office* (Jan. 28, 2003) (noting announcement by Wisconsin Governor Jim Doyle announcing an investigation of MCI for slamming complaints, including violations of the state’s No Call list); see also Amended Verified Motion for Enforcement of Order Granting Emergency Relief, *Illinois Bell Tel. Co. Complainant, vs. MCI WorldCom Communications, Inc., MCI Metro Access Transmission Services, LLC, and MCI WorldCom Communications, Inc. f/k/a MFS Intelenet, Respondents*, Docket No. 02-0443 (Ill. Commerce Comm’n filed Jan. 13, 2003).

revoked.” The Commission has certainly revoked licenses in the past for misconduct far less serious than WorldCom’s, where the harms to others in the industry were very much less grave.⁵⁵ As the Commission has emphasized, “violations of the Communications Act or the Commission’s rules are matters which are predictive of licensee behavior and directly relevant to the Commission’s regulatory activities.”⁵⁶ The fact that WorldCom has exhibited an “apparent continuing course of misconduct raises questions as to whether [it] possesses the requisite character qualifications to be and remain a Commission licensee.”⁵⁷

The Commission must certainly reject the argument that WorldCom is simply too big to be allowed to fail. WorldCom has *already* failed — spectacularly. The question now is how many more companies, creditors, shareholders, and employees will be dragged down into insolvency with it. Predictably, some investors are already buying up the heavily discounted WorldCom debt, betting that the Commission will stand aside, do nothing, and permit WorldCom to rise Phoenix-like from the ashes. But most analysts

⁵⁴ Section 312 of the Communications Act grants the Commission authority to revoke a license “for false statements knowingly made either in the application or in any statement of fact” to the Commission, or “because of conditions coming to the attention of the Commission which would warrant it in refusing to grant a license or permit on an original application.” 47 U.S.C. § 312(a). As the Commission has recognized, “[t]his same standard is applied to common carrier licenses.” *MCI Telecommunications Corp.*, 3 FCC Rcd 509, 512, ¶ 31 (1988), (citing *Character Policy Statement*, 102 F.C.C.2d at 1195, 1201).

⁵⁵ See, e.g., *Mr. Frank Battaglia, President, North American Broadcasting Co.*, Letter, 7 FCC Rcd 2345 (Mass Media Bur. 1992) (admonishing licensee for employer hoax broadcast even though station denounced broadcast, tired employees involved, and took other corrective measures); *Application of Northwestern Indiana Broadcasting Corp.*, Initial Decision of Administrative Law Judge John H. Conlin, 65 F.C.C.2d 73 (1976) (station’s renewal license denied after discovery that general manager/vice president submitted false information to the Commission); *KWK Radio, Inc.*, 34 FCC 1039 (1963) (revoking broadcast license due to fraud by station’s general manager in conducting a “treasure hunt” contest), *aff’d*, *KWK Radio, Inc. v. FCC*, 337 F.2d 540 (D.C. Cir. 1964); *Eleven Ten Broad. Corp.*, Decision, 32 FCC 706, 708-09, ¶¶ 6-7 (1962) (denying renewal in part because of log alterations made by station employee), *aff’d sub nom. Immaculate Conception Church v. FCC*, 320 F.2d 795 (D.C. Cir. 1963); *Carol Music, Inc.*, Decision, 37 FCC 379, 380, ¶ 3 (1964) (adopting in relevant part initial decision revoking license based in part on refusal by station manager to furnish information requested by the Commission).

⁵⁶ *Brewer*, 16 FCC Rcd at 5674, ¶ 12

⁵⁷ *Id.* at 5671, ¶ 1

agree that that would be the worst possible outcome for the industry as a whole. The “bigger danger lies in the aftereffects of WorldCom’s bankruptcy on other long-distance telecom companies,”⁵⁸ industry observers recognize. They decry Chapter 11’s “strong bias toward the continuation of unprofitable businesses, . . . when the most efficient outcome for the industry and the economy is liquidation.”⁵⁹ Bankruptcy will allow WorldCom to shed most of its debt, and thus a large fraction of its operating costs, and thus drop prices. “[C]ompanies that have operated ethically and within the law ‘are going to have a very difficult time competing effectively.’” Competitors may well have to dive into bankruptcy protection to get their costs in line — “[t]hey have to have a level playing field.” “[L]etting companies die would exhaust a lot of that capacity.”⁶² WorldCom’s survival, in short, threatens the health of the industry far more than its demise. As EMG concludes, “the chances that WorldCom’s demise will cause harm to the telecommunications sector are non-existent.” In any event, the prospects of such a demise certainly provide no excuse for failing even to conduct an investigation.

The Commission must also reject the argument that **all** the bad apples have now been cast from the barrel. At this point in time, the Commission certainly has no basis for concluding as much, nor will it have any such basis until it completes a comprehensive investigation of its own. WorldCom is a very large conglomerate. Its top

⁵⁸ Kevin Maney & Andrew Backover, *WorldCom’s Bomb*, USA Today, July 22, 2002, at B1.

⁵⁹ Lahart, *supra* note 23.

“Patrick Thibodeau, *Bankruptcies Could Trigger Price War*, Computerworld (Oct. 28, 2002) (quoting Brian Adamik, President and CEO of The Yankee Group), at <http://www.computerworld.com/managementtopics/xsp/isptelecom/story/0,10801,75419,00.html>).

⁶¹ Maney & Backover, *supra* note 58.

⁶² Lahart, *supra* note 23.

⁶³ EMG Report, at 11.

managers will have made thousands of decisions to hire, promote, **and** reward other, lower level managers over the past several years. The Commission does not know how many of those individuals bought, sold, and profited from WorldCom's inflated stock prices, during the years when the corporation's frauds went wholly unnoticed – apparently – by the many hundreds, if not thousands, of employees engaged in the day-to-day management of the company's businesses and b o o k ~ ~~The~~ Commission does not know how many of those same individuals may have known, or strongly suspected, that something was seriously awry, but opted to look the other way because their own bonuses, continued employment, and stock options depended on not questioning, not knowing, and not blowing the whistle.

The Commission needs to know. It has emphasized in the past that a company's top management cannot evade responsibility for the unauthorized misconduct of low-level employees.⁶⁵ The obvious logic for that position is that problems lower down in the

⁶⁴ An instructive comparison is possible, however, with the Commission's recent MobileMedia license revocation proceeding, which centered on false reports of the construction of facilities. In that case, the Commission conducted a comprehensive investigation and had in hand the target company's own admissions "that certain former members of [its] senior management were actively involved in the misbehavior." But the Commission nevertheless concluded that "it remains unclear which other officers, directors, and senior managers knew about or condoned the wide-scale pattern of misbehavior." The Commission therefore extended certain proscriptions to all "individuals within the scope of this proceeding," which it defined to include all "former or current" "officers, directors and senior managers." MobileMedia was required to supply "a list of all such persons," *i.e.*, all "potential wrongdoers." That list started out with 91 names, and was then shortened to 43 — for a company — MobileMedia — that was one-fiftieth the size of WorldCom. Compare MobileMedia Corp. Form 8-K (SEC filed July 7, 1997) (1996 revenues of \$641 million), with WorldCom, Form 10-K405 (SEC filed Mar. 13, 2002) (2001 revenues of \$36 billion).

⁶⁵ See, e.g., *Russellville Educational Broadcast Foundation, Letter*, 14 FCC Rcd 11208, 11209 (1999) ("Licensees cannot be excused from responsibility for the acts of their employees."); *Hemmingford Media, Inc., Order of Forfeiture*, 14 FCC Rcd 2940, 2941, ¶ 7 (1999) ("[The Commission] remind[s] respondent that the responsibility for compliance with the terms of . . . [the licensee's] license rests solely and exclusively with the licensee."); *Zapis Communications Corp.*, Memorandum Opinion and Order, 7 FCC Rcd 7859, 7859, ¶ 5 (1992) ("[I]t is well established that an employer remains responsible for the actions of its employees."); *Rocket Radio, Inc.*, Memorandum Opinion and Order, 70 F.C.C.2d 413, 424-425, ¶ 15 (holding licensee responsible for an employee's false affidavit that was submitted to the Commission); *Ned N. Butler and Claude M. Gray, D.B.A. The Prattville Broadcasting Co., Prattville, Ala.*, Decision, 4 F.C.C.2d 555, 563-64, ¶ 20 (1966) ("The Commission has repeatedly refused to absolve a

management hierarchy reflect problems higher up, and punishing the enterprise as a whole is the only way to ensure that top management cultivates a supervisory culture that takes responsibility for misconduct throughout the company.⁶⁶ In WorldCom's case, however it was the managers themselves that were – for many years – perpetrating the fraud. If principles of vicarious responsibility and liability are to apply at all, they must surely apply here. Before it can apply those principles intelligently, the Commission must find out just how far the responsibility for this debacle extends. Conducting a full investigation of WorldCom will help to foster a corporate culture in the industry in which the importance of making truthful representations is appreciated at every level of the corporation.

As the Commission has recently noted, “deterrence is an important element of the character qualifications process.” and helps send a message that will help prevent “future misconduct.””” The Commission must now decide whether it will send that message to the industry, or whether it will sit idly by while the largest fraud in corporate history has been perpetrated on the industry and the consumers that it is charged to protect.

IV. The Commission Need Not Defer to the Bankruptcy Court in Exercising Its “Public Interest” Authority.

Under well-settled precedent, the Commission owes no deference to the bankruptcy court in deciding, after a full investigation, whether revocation of

licensee of responsibility for deceptions practiced by his employees, and in instances of serious transgressions has imposed sanctions upon the licensee notwithstanding his professed lack of knowledge.”).

⁶⁶ See *Character Policy Statement*, 102 F.C.C.2d at 1218, ¶ 78 (“A corporation must be responsible for the FCC-related misconduct occasioned by the actions of its employees in the course of their broadcast employment. To hold otherwise would, inter alia, encourage corporate owners to improperly delegate authority over station operations in order to ‘neutralize’ any future misconduct.”).

⁶⁷ *James A. Kay, Jr. : Licensee of One Hundred Fifty Two Part 90 Licenses in the Los Angeles, California*, Memorandum Opinion and Order, 17 FCC Rcd 8554, 8558, ¶ 9 (2002) (citing *Character Policy Statement*, 102 F.C.C.2d, at 1128, ¶ 103).

WorldCom's licenses or some other appropriate sanction will best serve the *public* interest here." A bankruptcy court looks to the immediate interests of creditors and employees, but has no mandate to evaluate broader impacts on the industry as a whole.

As a general proposition, a licensee may not transfer facilities involved in a hearing concerning its character qualifications unless it is found qualified to remain a licensee.⁶⁹ Under the Commission's **Second Thursday** doctrine, however, when such a licensee has gone into bankruptcy, the station license may nevertheless be assigned (usually by the bankruptcy trustee), "if individuals charged with misconduct will have no part in the proposed operations and will either derive no benefit from favorable action on the [assignment or transfer] application or will receive only a minor benefit which is outweighed by equitable considerations in favor of innocent creditors."⁷⁰ The **Second Thursday** doctrine merely "accommodates the policies of the federal bankruptcy law with those of the Communications Act."⁷¹

Moreover, the key licenses that WorldCom holds are quite different from those involved in a revocation of a broadcast or PCS license. WorldCom's licenses have no value in and of themselves, Section 214 licenses, together with ancillary point-to-point microwave and other wireless licenses of similar character, are not broadcast or PCS licenses; these licenses are not issued to address problems of inherent scarcity, and in any event, the Commission can readily commit itself to facilitating the orderly transfer of assets to new, licensed owners of WorldCom's network facilities.

⁶⁸ See, e.g., *Magic Valley Broadcasting, Inc.*, Hearing Designation Order, 1985 FCC LEXIS 2850, n. 7 (1985); *Peoria Community Broadcasters, Inc.*, Memorandum Opinion and Order, 79 FCC 2d 311, 321 (1980).

⁶⁹ See *Jefferson Radio Co. v. FCC*, 340 F.2d 781, 783 (D.C. Cir. 1964).

⁷⁰ *Second Thursday Corp.*, Memorandum Opinion and Order, 22 F.C.C.2d 515, 516, ¶ 5 (1970).

⁷¹ *LaRose v. FCC*, 494 F.2d 1145, 1147 n.2 (D.C. Cir. 1974).

Nor does the Supreme Court's recent decision in *Nextwave* in any way affect the Commission's enforcement authority, including its ability to revoke licenses for misconduct, while WorldCom is in bankruptcy. The Supreme Court stressed that for section 525 of the bankruptcy code⁷² to come into play "the failure to pay a dischargeable debt must *alone* be the proximate cause of the cancellation."⁷³ That is plainly not the case here. WorldCom's Section 214 licenses are not subject to any dischargeable debt. The sole basis for their revocation – if the Commission, after a full investigation, reaches such a decision – would be WorldCom's egregious, unlawful and fraudulent misconduct.

A bankruptcy trustee can thus seek, and the Commission can readily approve, the transfer of WorldCom's licenses in the course of an orderly sale of WorldCom's network assets. In revoking WorldCom's licenses, the Commission will not "effectively depriv[e] creditors of significant recovery of their money,"⁷⁴ — it will simply force whatever recovery is possible to come from an orderly sale of assets to altogether new corporate management.

"See 11 U.S.C. § 525(a) ("[A] governmental unit may not... revoke... a license... to... a debtor... solely because such... debtor... has not paid a debt that is dischargeable in the case.").

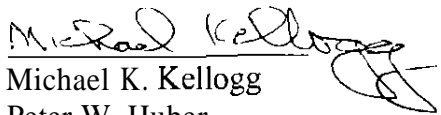
⁷³ *Nextwave*, 2003 U.S. LEXIS 1059, at *3 (emphasis added).

⁷⁴ *LaRose*, 494 F.2d at 1145.

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